CONCEALMENT OF ASSETS IN BANKRUPTCY CASES.

ALTHOUGH section 29 of the Bankruptcy Act has made it a crime in a debtor to have "concealed, while a bankrupt or after his discharge, from his trustee any of the property belonging to his estate in bankruptcy," experience has shown that this is one of the usual incidents to be expected in the ordinary dishonest bankruptcy case. While the commercial community demands a criminal prosecution in an extraordinarily flagrant case of concealing assets, or where there is an unusual succession of such dishonest failures in a locality, yet the average merchant's primary interest is merely to recover such assets so as to make his dividend from the estate as large as possible. He is willing that such dishonest bankrupts shall be punished, but he will usually forego this desire if the bankrupt tempts him to accept a composition by giving him a few cents on the dollar more than "the assets in sight" will yield. While this may be due in part to a lax commercial standard amongst our merchants, it is also due to two definite faults in the administration of the bankruptcy law by the courts themselves. A composition proceeding under section 12 enables creditors to obtain their dividend more speedily than through the regular administration of a bankrupt estate. In large part this is inevitable. In part, however, it is due to a failure of the administrative part of the District Courts to compel the payments of dividends as often and as speedily as is contemplated under section 65 (*b*). But the principal cause of this is in the attitude of many of the courts in demanding a standard of proof concerning concealed assets, which is commercially impractical and legally unsound.

Very correctly the courts have generally laid it down as a fundamental axiom in this class of cases that they will not make an order on the bankrupt to turn over to his trustee secreted assets which he is alleged to be wrongfully withholding unless they are prepared to follow up a non-compliance with the same by a further order committing him for contempt of court.[1] The result, therefore, is that the

[1] American Trust Company *v.* Wallis, 126 Fed. 464; *In re* Rosser, 101 Fed. 562, 4 A. B. R. 153; *In re* Adler, 129 Fed. 502, 12 A. B. R. 19; *In re* Walder, 152 Fed. 489, 16 A. B. R. 41.

inquiry concerning assets wrongfully concealed by a bankrupt from his trustee naturally divides itself into two distinct lines of investigation. The first is whether assets have been secreted by the bankrupt, and if so what they are. The second, what can be done by the bankrupt to procure their return.

There is very little real difficulty or difference of opinion in relation to this first question. If the creditors or the trustee establish by a fair preponderance of the evidence the facts from which a concealment of assets is to be deduced the court draws the natural inferences just as in any ordinary legal proceedings. On the other hand there is a very definite and irreconcilable conflict of opinion as to what the court will require from the complainants in the way of proof of the bankrupt's ability to comply with an order to return assets which the court is willing to believe have been wrongfully withheld from the bankrupt estate. This divergence of points of view and its consequent differences in the administration of the law by the various District Courts as well as the diversity of opinion between the several Circuit Courts of Appeal can best be illustrated by means of a typical case. In an exceedingly well written report a referee in bankruptcy submitted to the district judge for the Northern District of Georgia[1] the following findings of facts: 1. The bankrupt who was a country merchant in Georgia destroyed his original invoices of merchandise. 2. The bankrupt failed to produce the original book kept by him in his business, and offered no adequate explanation for its non-production. He produced a book purporting to be a copy thereof made under such circumstances as to justify the belief that it did not fairly set forth his business transactions. 3. A short time before the filing of the petition in bankruptcy the bankrupt was possessed of a stock of merchandise, so large as to attract attention. Persons qualified to judge of its value estimated it to be worth about $20,000, which value was corroborated by statements of the bankrupt made before the bankruptcy proceedings. 4. The net amount of the goods, when the receiver took charge, was found to be only $4423.53. 5. The sales made prior to the bankruptcy did not account for the discrepancy. 6. There was evidence that considerable merchandise had been moved from the bankrupt's store out of business hours, and there was strong suspicion that on several occasions during the night, boxes had been moved

[1] Report of W. E. H. Searcy, Jr., quoted *In re* Rogowski, 166 Fed. 165, 21 A. B. R. 553.

from the bankrupt's store to that of his son-in-law a short distance away. A small part of such goods had been recovered by a receiver from the son-in-law. Without taking into account a considerable shortage of cash, the conclusion was reached that the bankrupt was withholding, secreting, and concealing from the trustee, merchandise. "That said merchandise withheld, secreted, and concealed by the bankrupt is within the possession or custody, or in the power and control of the said A. Rogowski, bankrupt."

After reading this report no reasonable business man or lawyer with commercial experience can have any doubt about that case. Yet on technical objections the report was recommitted to the referee for "a more specific finding." He then submitted a further report.

"I further find that there is no testimony which would authorize a finding that any part or all of said merchandise consisted of dry goods, or notions, or clothing or shoes, or any other particular class of merchandise, other than to find and say that it must of necessity have consisted of such articles of merchandise as were bought and carried in stock by the bankrupt. This is as full, definite and particular description of the merchandise as may be made from the evidence in the case."

Thereupon the district judge dismissed the trustee's petition for an order on the bankrupt to deliver up to him secreted assets because "the referee did not point out in this report where any of the goods were or locate them in a definite way."

Here, then, is a case where shortly before a failure the bankrupt had a considerable stock of merchandise, while after bankruptcy the assets are found to be but a small part of what they had been. Nothing in the ordinary course of business explains this. Circumstances irresistibly indicate a fraudulent secretion of property. No one except the bankrupt can say where the property now is. He either remains silent or offers no adequate explanation.

One view is pithily summarized and tersely put by Judge Sanborn.[1]

"The rule by which this issue is to be determined is that the property of the bankrupt estate traced to the recent possession or control of the bankrupt is presumed to remain there until he satisfactorily accounts to the court for its disappearance or disposition. He cannot escape an order for its surrender by simply adding perjury to fraudulent concealment or misappro-

[1] Boyd *v.* Glucklich, 116 Fed. 131, 8 A. B. R. 393.

priation. It is still the duty of the referee and of the court, notwithstanding his oath and testimony, if satisfied *beyond a reasonable doubt* that he has property of the estate in his possession or under his control, to order him to surrender it to the trustee, and to enforce that order by confinement as for contempt." [1]

The opposing line of decisions is fairly represented by the opinion of the Court of Appeals for the Fifth Circuit referred to in the Rogowski case: [2]

"It follows unquestionably that an order imprisoning a bankrupt for contempt for failure to obey a decree to pay money or surrender goods into court, is erroneous as a matter of law, where the bankrupt by sworn answer denies that he has the money or goods, and it does not appear clearly and affirmatively from the record, notwithstanding his denials, that he has the power to comply with the decree. The bankrupt is at least entitled to that much protection if indeed the courts are to refuse to follow the wise rule of the common law which makes the sworn denials of the answer sufficient defence to the contempt proceedings, leaving the question of the truth of the answer to be contested in a prosecution for perjury."

Or perhaps this attitude of the courts is expressed more strikingly by the District Court of South Carolina,[3] which says that "the court in making an order to commit a bankrupt to jail as for contempt for failure to account for goods and money, should be governed by the same considerations which would influence a jury in a criminal prosecution, giving to the bankrupt the benefit of any reasonable doubt."

So, whichever of these opinions is followed, the conclusion inevitably is that no order is to be made on the bankrupt unless the court is satisfied *beyond a reasonable doubt* that the bankrupt has the secreted assets in actual possession or control. The proceeding to compel a restitution of assets with a possibility of punishment for contempt is perhaps in the majority of jurisdictions [4] regarded as "criminal in its character," and a conclusion against the bankrupt is to be reached only when the evidence induces such belief beyond a reasonable doubt.

The short answer to such arguments is that such proceedings are not in their nature criminal. In the courts of chancery an attachment

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[1] *In re* Gerstal (Ill. S. D.), 123 Fed. 166, 10 A. B. R. 411; *In re* Kane (Pa. M. D.), 125 Fed. 984, 10 A. B. R. 478; *In re* Dewell (Mo. W. D.), 100 Fed. 633, 4 A. B. R. 60.

[2] Samuel *v.* Dodd, 142 Fed. 68, 16 A. B. R. 163.

[3] *In re* Switzer, 140 Fed. 796, 15 A. B. R. 468.

[4] Moody *v.* Cole (Me.), 148 Fed. 295, 17 A. B. R. 818; *In re* Goldfarb (Ga.), 131 Fed. 643, 12 A. B. R. 386; *In re* Anderson (S. C.), 103 Fed. 854, 4 A. B. R. 640.

to enforce obedience to an order to pay money or to surrender property is to be regarded as a civil execution for the benefit of the equitable owners of the fund.[1] "If the fact that a failure to comply with the order of the court may result in imprisonment of the respondent for contempt makes it a criminal case, many proceedings, and especially proceedings in courts of equity, would have to be treated as criminal proceedings. The failure on the part of the defendant to execute a conveyance decreed by a court of equity in a proceeding for a specific performance may be enforced by imprisonment as for contempt. Refusal to answer interrogatories in a bill of discovery, refusal to pay alimony in a divorce suit, disobedience to a writ of mandamus or violation of an injunction may result in such punishment; but no one will contend that for this reason such proceedings are in the nature of criminal actions. The punishment for contempt in bankruptcy proceedings is simply for disobedience of the judgment of the court after it is found that the respondent has money or property belonging to the bankrupt estate in his possession or under his control, and, although able to comply with the order of the court, wilfully refuses to do so. These provisions in the bankruptcy act, authorizing courts of bankruptcy to enforce obedience to their orders by punishment as for contempt, are neither novel nor unusual. They were included in every bankruptcy act, and similar provisions have been enacted by almost every State in the Union. . . . In proceedings supplemental to or in aid of executions, courts are authorized by these statutes to enforce the surrender of assets subject to executions, and for this purpose may commit to jail any person refusing to comply with such order." [2]

The rule requiring that the complainant shall establish "beyond a reasonable doubt" the bankrupt's possession or control over the secreted property is only another aspect of this error of regarding contempt proceedings as criminal prosecutions. If the proceedings are not criminal there is of course no such rule of evidence. However, many courts which stop short of calling contempt proceedings criminal, still cling to this "beyond a reasonable doubt" rule. While there is more or less authority for this, yet the weight of authority is clearly that the rule of evidence is no more stringent on such issues than upon any other issues of fact in chancery. That amount of evidence which will satisfy the conscience of the court is sufficient. The ordinary rule

[1] *In re* Alphin & Lake Cotton Co., 134 Fed. 477, 14 A. B. R. 197.

[2] *In re* Alphin & Lake Cotton Co., *supra.*

of the "fair preponderance of the evidence" is enough to discharge the burden of proof on the complainant in contempt proceedings.[1]

What has in part misled the courts is an excessive caution to prevent a harsh or abusive use of the provisions of the Bankruptcy Act by over-zealous creditors against their debtors. "Creditors who sell to persons of doubtful or unknown financial standing, and of unknown or suspicious character for integrity, and who, by their own lack of ordinary diligence, have become the victims of fraud, should proceed for redress under the ordinary methods of legal procedure, and cannot expect to use, as an ordinary agent in the collection of debts, the power to imprison for contempt, which is to be applied only in cases of contumacious resistance to the orders of the court." [2] In part too this error is due to the failure to recognize that the Bankruptcy Act itself has imposed upon the bankrupt an absolute duty to "submit to an examination concerning the conducting of his business, the causes of his bankruptcy, his dealings with his creditors and other persons, the amount, kind, and whereabouts of his property," etc.[3] The dispositions of his assets must necessarily be peculiarly within the knowledge of the bankrupt. His silence on the subject can admit of but one interpretation. It is of itself the most significant of evidence. While an explanation that does not explain is even worse.

Common sense would ordinarily dictate that "the question is whether it is sufficient for the bankrupts to state that they have not the property. If they have not the property, they should tell what they did with it. If they cannot do this, the court would be justified in finding that they still had it." [4] "If the money is once placed into the hands of a respondent, the burden is upon him to make some reasonable explanation of what has become of it or at least that it has ceased to be in his possession or under his control at the time the order to turn it over was made." [5]

This idea of shifting the duty of producing further evidence to explain or rebut evidence already introduced, which, if unexplained or uncontradicted, would be sufficient to establish a *prima facie* case is to-day common enough in many other classes of cases. Thus in the

[1] Rapalje Contempt Par. 126; *In re* Cole, 163 Fed. 180, 20 A. B. R. 761; Verplank *v.* Hall, 21 Mich. 470; Stuart *v.* Stuart, 123 Mass. 370; Drakesford *v.* Adams, 98 Ga. 722.

[2] *In re* Davidson, 143 Fed. 173, 16 A. B. R. 337.

[3] Section 7 (9).

[4] Matter of Levy, 142 Fed. 442, 15 A. B. R. 169.

[5] *In re* Alphin & Lake Cotton Co., 134 Fed. 477, 14 A. B. R. 194.

tort cases of daily occurrence in our courts, evidence of an accident may be introduced of such a nature that our common experience indicates that it would not have happened if there had not been negligence. Some courts have said that this makes out a *prima facie* case for the plaintiff, others say that the negligence is inferred or presumed. "But whichever form of expression may be chosen, *prima facie* evidence in legal intendment means evidence which if unrebutted or unexplained is sufficient to maintain the proposition and warrant the conclusion to support which it is introduced." [1]

This rule of law is no less applicable to the class of cases under consideration. "The presumption of law in such cases, in the absence of satisfactory explanation, is that the property traced to the hands of the bankrupt a short time prior to the suspension of business remains in his hands, and the bankrupt must answer therefor." [2]

So even though imprisonment for contempt may be the ultimate outcome of a petition to require the return of secreted assets by a bankrupt, still the correct rule of law is that applied in ordinary chancery suits. A proceeding to procure the return of concealed assets is neither criminal nor quasi-criminal in its nature. Such proceedings retain their character as civil throughout. The ordinary rules of evidence apply, and the ordinary inferences and presumptions are to be made. The plaintiff sustains his contentions if each material allegation is established by a fair preponderance of evidence. The bankrupt who has a statutory duty to make true and full disclosure of his property and his dealings, does not stand protected by any presumption of innocence nor is he entitled to any special protection from the court. Though it is of course true that the court should exercise with caution its extraordinary power to punish for contempt, where a proper case is presented by the evidence, a court is not to allow itself to be deterred by the consequences.

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[1] Carroll *v.* Boston Elevated R., 200 Mass. 527, and cases there cited. See also Wigmore Evidence, chap. lxxxvi.

[2] *In re* Rogers Dry Goods Co., 133 Fed. 100, 13 A. B. R. 266.